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Submitted to the Subcommittee on Oversight and Investigations
United States House of Representatives
On Competition in the Cellular Telephone Service Industry
October 12, 1995

Mr. Chairman and Members of the Committee:

Good morning. I am pleased to be here to testify today about the Department of Justice's perspective regarding current and future competition in the wireless telephone service industries. I applaud this Subcommittee and its leaders for their attention and important interest in encouraging competition in these vital markets. Forging strong competition in the important telecommunications industries is also one of the Administration's foremost priorities, because increased competition in telecommunications will benefit consumers, spur economic growth and innovation, promote private sector investment in an advanced telecommunication infrastructure and create jobs.

I would like to begin today by briefly laying out the Department's perspective on competition in the wireless telephone service markets, as well as outlining what the Department has done to protect and encourage competition within these markets. I will also briefly address our views as to future competitive issues that will likely confront both the Congress and the Department in its enforcement role. Following this testimony, I will be happy to respond to any questions you might have.

COMPETITION IN WIRELESS TELEPHONE MARKETS

The wireless communications industries encompass a vast array of one-way broadcast and two-way communications services. Indeed, wireless telephone communications services include not only what we would traditionally think of as mobile phone service, i.e., wireless common carrier access to the public switched telephone network, but also numerous other services such as wireless signalling and data transmission services. Because the Department of Justice's work concerning the wireless telecommunications industries is based on competitive considerations, we focus not on particular technologies or radio spectrum allocations, but rather on the services offered by the various technologies or over the various transmission media, and their role in the marketplace. In the area of wireless telephone services, telephone service over the "cellular" radio frequencies is the most common and recognizable, but other technologies operating on other radio frequencies have the potential to offer similar and competitive services. Referring to a "cellular" service market is thus something of a misnomer, particularly in light of expected future capabilities of other mobile radio systems currently being developed. However, the term has become almost synonymous for wireless because cellular telephone service has traditionally been the only widely available wireless telephony service of its kind.

The Cellular Duopoly

Commercial cellular telephone service has grown at an incredible rate from roughly 92,000 subscribers in 1984 to over 24 million last year. This illustrates the growing importance of wireless telephone services in our everyday lives. However, while the technology and service offerings to subscribers have changed dramatically, the overall industry structure has remained relatively stagnant. In 1981, the FCC decided to authorize only two cellular licenses -- a "B-side" license given to the local telephone companies, and an "A-side" license for companies unaffiliated with the telephone companies -- for each of the 734 local cellular market areas in the United States.

Economic theory and experience teach that markets with only two competitors and legal barriers preventing additional entry will result in only limited competition. This is consistent with the Department's experience in the wireless markets. The Department has consistently voiced strong concerns over the cellular duopoly structure -- even before this structure was created. We continue to believe that the markets for wireless telephone service, as controlled by the cellular duopolists in each area, are not fully competitive and that these markets need additional wireless service providers in order to become adequately competitive. Moreover, the Department has consistently rejected claims that landline telephone service, wireless paging services, or two-way mobile dispatch services are now sufficiently substitutable with traditional cellular service

to provide adequate competitive restraints on the duopoly cellular providers. Numerous other federal agencies, including the Federal Communications Commission ("FCC"), the General Accounting Office ("GAO"), and the Federal Trade Commission, have reached similar conclusions that the market for cellular services is not fully competitive. See, e.g., First Report, *In the Matter of Implementation of Section 6002(B) of the Omnibus Budget Reconciliation Act of 1993*, Annual Report and Analysis of Competitive Market Conditions with Respect to Commercial Mobile Services (CC Docket No. 95-317, at ¶ 65-66) (August 18, 1995); Report to Hon. Harry Reid, U.S. Senate, *Concerns About Competition in the Cellular Telephone Service Industry* (GAO 1992); Comment of the Staff of the Bureau of Economics of the Federal Trade Commission, *In re Bundling of Cellular Customer Premises Equipment and Cellular Service* (CC Dkt. No. 91-34) (July 31, 1991).

In an effort to facilitate competitive entry by the "A-side," non-telephone company cellular licensees, the FCC effectively created the possibility of a "wholesale" cellular market by requiring cellular carriers to offer potential "resellers" of their service rates that are no less favorable than the lowest "bulk" rate offered to other large customers. In the telecommunications industry, resale requirements have proven helpful in the past as a way to enable new entrant competitors to provide market-wide service while constructing new competitive facilities. Thus, most of the A-side cellular licensees were

able to begin competitive service much earlier than would have otherwise been possible, by reselling service of the telephone-company "B-side" cellular licensees, which were awarded and constructed first. This reduced the B-side's first-mover advantage. Similarly, following the Department's 1982 lawsuit separating AT&T's long distance service and manufacturing operations from its local Bell Company exchange monopolies, MCI and Sprint both extensively resold AT&T long distance telephone service while constructing their own competitive nationwide long distance networks, increasing overall long distance competition dramatically.

Unfortunately, resale has not been as successful or effective in current cellular service markets. We agree with our colleagues at the FCC, GAO and other federal agencies in concluding that current cellular reseller arrangements do not provide effective competition to the entrenched cellular duopolists. Because their "wholesale" service costs are completely controlled by the facilities-based carriers, resellers have not typically been able to constrain the incumbent carriers' prices. Nor can resale currently be helpful to enable a competitor to develop a customer base while becoming a facilities-based competitor because of restrictions on new entry. While resale still may be helpful, the best solution is the rapid assignment of new spectrum licenses through the FCC auction process.

Potential Competitive Impact of PCS

In 1992, the FCC took the initiative to infuse new competition into the wireless telephone service markets by beginning the process of reallocating blocks of radio spectrum for Personal Communications Services or "PCS" systems. One view of PCS within the telecommunications industry envisions that individuals, instead of sending voice and data communications from stationary sources, will be able to send such communications from mobile points, with telephone numbers attached to individuals rather than to stationary sources. The FCC designed the PCS spectrum allocation to provide a "wide array of mobile, portable and ancillary communications services." The Department submitted comments in these PCS rulemaking proceedings, and the FCC adopted a number of the Department's recommendations, such as:

1. to assure that each PCS licensee have enough usable radio spectrum to provide efficient wireless services and potentially to compete with incumbent cellular carriers;

2. to distribute the PCS licenses in an auction format and allow for a secondary license market (subject to limits on multiple holdings and the operation of the antitrust laws);

3. to allow firms to acquire additional non-overlapping licenses to allow the market to determine and achieve the most efficient service area size; and

4. to allow the market participants to determine for themselves the types of services to offer, rather than mandating a particular use for the spectrum.

I would also like to commend Congress for its active support in promoting auctions as a format for distributing the PCS

licenses. Wholly apart from the benefits to the United States Treasury, we believe that auctions are the best method for assuring that the licenses go to those market participants who are the most likely to maximize their value.

The FCC has very quickly and effectively implemented an auction scheme for the distribution of PCS spectrum. In June, the FCC announced the initial licensees based on the results of the first of several PCS frequency auctions -- the large 30 MHz "A" and "B" spectrum blocks. Although large telecommunications joint ventures and companies dominated the auction, this was not unexpected given the tremendous capital investment and industry expertise required to develop and exploit the new PCS systems. The biggest auction winners include large individual telecommunications companies like AT&T, GTE and Pacific Telesis, as well as telecommunications joint ventures. These joint venture or bidding consortia include *"PCS Primeco,"* a PCS joint venture made up of Bell Atlantic, NYNEX, US West, and Airtouch; and *"WirelessCo, LP,"* a PCS joint venture made up of Sprint and three of the largest cable companies: TCI, Cox Cable, and Comcast Corporation. The Department closely monitored the initial A & B block auction to protect the competitive integrity of the auction itself, and to ensure a competitive industry structure thereafter. The FCC wisely restricted the amount of overall spectrum that may be held by existing cellular service providers in their service areas, in order to enhance the

prospect that the new spectrum will be used to compete with existing cellular providers.

The FCC, the Department, the NTIA, and others in the industry hope that the "broadband" PCS service will include services currently offered by the incumbent cellular carriers and will infuse significant new competition into the wireless telephone services market. However, the potential impact of PCS is still largely unknown, because no systems in this newly allocated bandwidth are currently complete or operational. Moreover, there is no guarantee that all of the new PCS entrants will offer services that directly compete with those currently offered by cellular carriers, instead of offering other types of services, such as wireless data communications. Service offerings may well vary based on the underlying communications infrastructure (e.g., cable TV) available to the winning bidder(s).

Based on early indications from some of the winning bidders in the PCS auction, it appears that at least some of the new PCS licensees plan to offer a "cellular-like" service. Also, it is possible that some aspects of PCS technology may give new PCS entrants an edge over the older cellular systems. For example, new PCS systems are widely expected to use digital signals from the start, which might offer expanded capacity and other advantages over the analog signal systems still used by most cellular carriers. However, PCS technology also has potential disadvantages compared to cellular, and cellular has a

considerable first-mover advantage reflected in the embedded base of cellular phones. Thus, it is far too soon to claim an end to the cellular carriers' market power.

Potential Competitive Impact of ESMR

As in the PCS arena, the Department has actively supported efforts to create potential competition for the wireless telephone market -- and its cellular duopolies -- from other wireless technologies such as Specialized Mobile Radio or "SMR" dispatch services. SMR is currently used primarily to provide two-way communications between delivery trucks, taxis and other business vehicles and central dispatchers. Just last year, the Department completed a major investigation into a series of SMR company consolidations culminating in Nextel Communications' acquisition of Motorola's SMR business. Motorola and Nextel were two of the largest SMR spectrum license-holders and have committed billions of dollars in an effort to create a broad-based digital enhanced SMR or "ESMR" system by consolidating bandwidth in the 800 MHz SMR spectrum. This ESMR service could potentially provide competition for some or all of the current cellular service offerings and the future PCS services, and perhaps offer additional dispatch and data communications capabilities as well.

Following our investigation, the Department entered into a consent decree which allowed the parties to pursue their potentially procompetitive plans for a new cellular-like service, while still protecting existing competition and availability of

capacity for traditional SMR dispatch services. However, as with PCS, ESMR systems like the one being developed by Motorola and Nextel are still the start-up stage. It is still far too soon to say when, or even whether, such ESMR services may provide a widely available competitive alternative to the cellular duopolists.

Potential Competitive Impact of Other Technologies

Another potential competing wireless technology on the horizon is satellite-based wireless services, such as Low Earth Orbit satellites ("LEOs") and Geostationary Earth Orbit satellites ("GEOs"). However, there are no LEOs or GEOs currently in operation and this is not expected to change imminently. These may provide a competitive alternative in the future, but they do not do so now. The Department will continue to monitor the industry and its developments.

OTHER DOJ ACTIVITIES IN THE WIRELESS FIELD

Apart from new services on the horizon such as PCS and ESMR, the Department has also been active on other fronts in ensuring and promoting competition in the wireless telephone markets. Two of our most recent efforts have been the Department's investigation into the acquisition of McCaw Cellular by AT&T, and the Department's "Generic Wireless" waiver proceeding before Judge Greene under the 1982 AT&T consent decree.

In AT&T/McCaw, the Department fashioned a consent decree designed to allow the parties to pursue economic efficiencies and other potential procompetitive effects of their vertical

consolidation, while at the same time protecting competition in the cellular equipment and cellular long distance markets. Perhaps most significantly, the AT&T/McCaw decree mandates that all of McCaw's cellular properties convert to "equal access" and provide non-discriminatory interconnection to long distance companies, which may significantly increase competition in the cellular long distance market. Previously, McCaw, although it is the largest single provider of local cellular service, offered only resold AT&T long distance service to its customers.

Similarly, in the "Generic Wireless" proceeding under the Modification of Final Judgment, or "MFJ," in United States v. AT&T, the Department worked in proceedings before Judge Greene to remove the MFJ barriers and allow the Regional Bell Operating Companies to enter the wireless interexchange markets to compete with the long distance carriers, while at the same time maintaining key restrictions to ensure that, in spite of RBOC monopoly power, entry would proceed in a manner that would not raise a substantial possibility that the RBOCs could impede competition in long distance. In granting the generic wireless waiver in late April, Judge Greene added a condition, not proposed by the Department, which makes RBOC entry into the wireless long distance markets more difficult than proposed by the Department. We are currently working through proceedings in both the District Court and the Court of Appeals to achieve our original aim of allowing RBOC entry into these markets with appropriate safeguards.

COMPETITIVE ISSUES ON THE HORIZON

There can be no doubt that the wireless telephone service industry is rapidly changing and that the principal challenge confronting all telecommunications policymakers is to encourage greater competition throughout the wireless industry in a way that does not distort the marketplace or pose dangers to consumers. Ultimately, effective competition in wireless telephone service markets will provide the best protection against the leverage and high prices associated with market power. In addition to the questions I discussed earlier regarding the potential for new PCS, ESMR, or satellite-based wireless service providers to compete effectively in wireless markets, there are other significant competitive issues ahead, both for Congress and for the Department.

Perhaps the most pressing of these issues concerns the potential future impact of consolidation efforts taking place within the wireless and wireline telecommunications industries. We are closely following these consolidation efforts and recognize that large portions of the overall wireless telephone spectrum -- both cellular and PCS -- are controlled by telecommunications consortia such as AT&T/McCaw, PCS Primeco, and WirelessCo. In the initial PCS auction alone, these three entities (or their individual members) submitted winning bids in a total of 46 out of 51 market areas, and received 63 out of the total 99 individual licenses auctioned. This is not to suggest that such concentrations are inherently anticompetitive; indeed,

competing in this business requires very large capital investments and significant expertise, and wireless consortia may offer substantial procompetitive benefits. However, because these consolidations offer increasing opportunities for companies to become partners in some markets and competitors in others, the Department will continue to place a high priority on review of these consolidations.

Related to this issue of industry consolidation is the possibility that in the future, wireless telephone service might offer a competitive alternative to the local landline exchange monopolies. However, the Department does not believe that this is the case today. We must consider what effect, if any, industry consolidation will have on the incentives of the market participants to engage in such potential future competition with wireline. In addition, in the wake of consolidation efforts and other moves by companies to obtain universal coverage through a nationwide wireless "footprint," we must consider whether wireless telephone service competition, which is currently local in nature, will begin to shift to a broader regional or national basis.

CONCLUSION

I am proud that our country, this Congress, and the FCC have the courage to address the tough issues of ensuring vibrant competition in the wireless telephone service markets as well as telecommunications markets as a whole. The Department of Justice has long been active in promoting and protecting competition in

the wireless service markets, both through interagency cooperation with the FCC, and through strong and innovative enforcement actions. By continuing vigorous enforcement of the antitrust laws, and by using real competition and the strength of the open market as our guide, the Department hopes to work with Congress to assure that wireless telecommunications services will help the Nation to competitive prosperity in the 21st century.